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IN THE

Supreme Court of the United States

OCTOBER TERM 1935—No. 758.

INTERNATIONAL BUSINESS MACHINES CORPORATION,
Appellant,

against

UNITED STATES OF AMERICA.

APPELLANT'S REPLY BRIEF.

EDWARD CORNELL,
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MARTIN A. SCHENCK,
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In order to sustain the decree, the Government has found it necessary (and it is in reality necessary) to place two extreme and unprecedented constructions upon the meaning and application of the Clayton Act.

POINT I.

Appellant's keyboard cards are not the "goods of a competitor" within the terms or meaning of the Act. There is no express violation of the Act. The necessity of using a precise "keyboard" card as an operative part of the machine meets any possible argument that the spirit of the Act is violated.

Appellant specified as error that the Court erred in decreeing that the tying clauses are in violation of Section 3 of the Clayton Act (Specification 3, Appellant's brief, p. 7), and argued that the Act was not *in terms* violated, for the

reason that no covenant obligated the lessee not to buy the goods of a competitor and then proceeded to show the reasonableness of the restrictions within recognized precedent in order to meet any possible contention that the spirit of the Act was violated.

But the Government rests its case on the contention that the tying clauses "come within the express terms of Section 3 of the Clayton Act," (Government's brief, p. 2), argues that the appellant's acts fall "within the express prohibitions of Section 3" (Government's brief, p. 16) and urges that the Clayton Act in Section 3 "contains no implied exception in favor of tying clauses designed to protect the lessor's good will" (Government's brief, p. 9).

The construction sought to be placed upon the Act by the Government thus finds no room for any tying clauses, no matter how limited in scope or reasonable in effect and no matter what their necessity.

The Government's contention that the statute, which prohibits the leasing of machinery on condition that the lessee shall *not* use the *goods of a competitor,* is in terms violated by a lease of appellant's machines on condition that the lessee *shall* use *in operation thereof* keyboard cards *of the lessor,* is without precedent. It is a reversal of the Government's attitude not only in respect of these particular tying clauses, to which it has been a party for 30 years, but of the rule in *United States* v. *United Shoe Machinery Co.,* 264 Fed. 138, 167, from which it did not appeal and which it has not until this case questioned. It contradicts the construction placed upon the Act by this Court in *Sinclair Refining Co.* v. *Federal Trade Commission,* 261 U. S. 463, wherein it was held that the lease of a tank which limited lessee to use *in connection therewith* lessor's gasoline, *inasmuch as it did not limit lessee in respect of dealing in goods of a competitor,* was not within the letter of the Act. It is certain in this case that appellant's leases do not prevent lessees from using competing machines, and the cards or other appurtenances thereof.

We respectfully submit that the case at bar presents the strongest possible case for tying clauses and that unless they are recognized here under these particular and limited circumstances the Act will necessarily be construed as urged by the Government, as eliminating their possibility under all circumstances.

In *United States* v. *United Shoe Machinery Co.*, 264 Fed. 138, 167, the clause which was held not to violate the Clayton Act was a clause that the lessee should buy, from the lessor exclusively, at "the regular prices from time to time established by the lessor", all duplicate parts, extras, mechanisms and devices of every kind needed or used in operating, *repairing* or *renewing* the leased machinery. There was no necessity that the machine part have any relationship to the operation of the machine. A crank, a standard, a nut or bolt, entirely independent of the operative feature of the machine, if it was involved in repair or renewal, was held to have its justification in the tying clause.

In contrast, in the case at bar, the stipulation shows that the cards are operative parts of the machinery and that upon their precision and accuracy the operative result depends.

In the *United Shoe Machinery* case, even if the part covered by the tying clause happened to be operative in character, the effect of it not being up to standard was that a shoe might be improperly constructed. The error was immediately observable and involved inconsequential values.

In contrast, in the case at bar the error is hidden and involves inaccuracy of all variations of numerical extent in mechanical accounting made the basis of financial operations.

In the *United Shoe Machinery* case, the effect upon the good will of the lessor in the reputation of the machines was, in consequence of the nature of possible error and its obvious and open character, slight in comparison to the effect upon the good will of the appellant here wherein the cause of mathematical fault is difficult to trace.

It is for these reasons that the Government has found it necessary to secure from this Court a new construction of the Clayton Act which would prevent the lessor from limiting its lessee in respect to using the lessor's goods, regardless of justifying necessity recognized since the time the statute was passed.

The Government advances entirely fallacious palliatives to throwing open to the hazards of indiscriminate manufacture these necessarily precise keyboard cards. It is quite aside from the point that it is *possible* for someone to manufacture a proper card. The Government during an experience of thirty years has not found that someone. It has not dared to take that risk. It has manufactured its own cards by its own machines and processes.

It states that it is a reasonable inference, from the fact that appellant's lessees are large concerns, that lessees of such type will purchase cards "only after definite proof of their suitability" (Government's brief, p. 12), and states at p. 22 of its brief that it must be assumed that appellant's lessees will *test* carefully the performance and quality of the goods purchased for use in the expensive machines. Of course, the Government is appellant's largest customer, but the Government has never put itself in the hazard to which it is attempting to subject the rest of appellant's lessees. It has never purchased a tabulating card on the general market. And its suggestion that appellant's lessees will *test* the cards they purchase is a recognition of the necessity that lessees must themselves engage in manufacturing in respect of cards, which the stipulation states must be of special manufacture for this particular purpose. *There is no known way of electrically testing a card after it has been cut.*

POINT II.

The Clayton Act has no application where the commodity tied is a part of a combination patent of the lessor. The clause "whether patented or unpatented" as used in the Act has application to the leased machines but no application to keyboard cards.

The first extreme construction which the Government has attempted to place upon this Act would make the prohibitions of the Section applicable *to the lessor's own goods*, although the statute in terms is applicable only to goods of lessor's competitor. But the second extreme construction which the Government seeks to place upon the Act goes even a step further. For the Government argues that the Act applies even to the *patented goods of the lessor.*

The Government necessarily takes this position in an attempt to sustain the decree below which struck out from a consideration of the case the patents which the parties had stipulated read on combination machine and card.

The Government thus advances as the vital question in the case (its brief, p. 22):

> "Whether the Clayton Act applies to and renders illegal the tying clauses in its leases even though under the patent law such an infringement suit would lie."

It is thus a part of the Government's case to establish that the Clayton Act intends to bring contributory infringers of combination patents into free competition in respect of the patent monopoly. True, the public policy recognized in the patent law gives the patentee the right to sue them for contributory infringement but the *contradictory public* policy of the Clayton Act must, on the Government's novel construction, give such contributory infringers triple damages against the patentee.

From the standpoint of combination-patent law, these tying agreements merely obligate lessees (in their own protection and in the protection of the patentee in respect of the patent), to refrain from contributorily infringing lessor's combination-patents in the operation of the leased machine.

The phrase "whether patented or unpatented" is used but once in Section 3 and that is in relation to the goods or machinery leased. It has no relationship to the goods or machinery "of a competitor or competitors of the lessor".

POINT III.

The decree should be reversed and the petition in all respects save as covered by the consent decree, should be dismissed.

Respectfully submitted,

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